
30 Friedrich August von Hayek (1899–1992)

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Biographical note

Friedrich August von Hayek, a central figure in 20th-century economics and a representative of the Austrian tradition, 1974 Nobel laureate in economics, was born on 8 May 1899, in Vienna, then the capital of the Austro-Hungarian empire. Following military service as an artillery officer in World War I, Hayek entered the University of Vienna, where he attended the lectures of Friedrich von Wieser and obtained doctorates in jurisprudence (1921) and political science (1923). After spending a year in New York (1923–4), Hayek returned to Vienna where he joined the famous *Privatseminar* conducted by Ludwig von Mises. In 1927, Hayek became the first director of the Austrian Institute for Business Cycle Research. On an invitation from Lionel Robbins, he delivered four lectures entitled 'Prices and Production' at the London School of Economics in 1931 and subsequently accepted the Tooke Chair. He was a vigorous participant in the heated debates that raged in England during the 1930s concerning monetary, capital and business-cycle theories. Hayek was to become the only intellectual opponent of John Maynard Keynes. As an outgrowth of his participation in the debate over the possibility of economic calculation under socialism, the focus of Hayek's research shifted during the late 1930s and early 1940s to the role of knowledge and discovery in market processes, and to the methodological underpinnings of the Austrian tradition, particularly subjectivism and methodological individualism. In 1950, Hayek moved to the United States, joining the Committee on Social Thought at the University of Chicago. His research there engaged the broader issues of social, political and legal philosophy. He associated with such figures as Frank Knight, Milton Friedman, Aaron Director and, somewhat later, George Stigler. He returned to Europe in 1962, with appointments at the University of Freiburg, West Germany, and then, in 1969, at the University of Salzburg, Austria. However, in 1977, Hayek moved back to Freiburg. He died in that city on 23 March 1992.

Hayek was a prolific author, not only in the field of economics, but also in the fields of political philosophy, psychology, epistemology and legal theory. However, his contributions to social and political philosophy and to legal theory emerged, to a significant degree, as extensions of his scholarship in the field of economics and its methodological foundations. The present entry is concerned somewhat narrowly with the contributions of Hayek in the field of legal theory.

Epistemological foundations

In retrospect and with the benefit of hindsight, it is apparent that Hayek's approach to the social sciences is rooted in a physiologically derived epistemological basis, the foundation of which he worked out during the 1920s. It was further developed in the time thereafter and finally published in 1952 as *The Sensory Order*. Although the book has for a long time been neglected, several commentators have recently recognized its importance (Bouillon, 1991; Streit, 1993). Hayek himself had already pointed out that his work on *The Sensory Order* had greatly helped him in developing his conception of evolution and of a spontaneous order and in analysing the methods and limits of our endeavours to explain complex phenomena (Hayek, 1979, pp. 199–200, fn 26). One of the central arguments of *The Sensory Order* is that our perception of the world around us is theory-guided or conjectural, in the sense that it is informed by a pre-existing system of classification – or set of classificatory dispositions – which is itself the product of a kind of 'learning', the outcome of an evolutionary process that can be said to reflect the accumulated 'experience' of the species. Thus Hayek's views as expounded in *The Sensory Order* come close to some of the tenets of what later became known as 'evolutionary epistemology'. In fact, Hayek's work can be interpreted as a systematic elaboration of the consequences that follow from an evolutionary epistemology for the issue of socioeconomic–political organization. His main subject is the social dimension of the knowledge problem, the problem of social learning; that is, the nature of the process by which knowledge is accumulated and utilized in society.

Hayek's concept of perception as classification has a systematic counterpart in his concepts of rules and rule-following behaviour (see also Hayek, 1967, pp. 43–65). Our perception and our behavioural responses to situations are both a matter of classification. Both are abstract in the sense that we respond not to the unique properties, but to typical features of situations with certain kinds of actions. In both realms learning is a matter of reclassification. If at the level of our cognitive apparatus the existing classification system generates expectations which are disappointed, there will be a tendency for the mind to reclassify experience. The mind will rearrange sensory experiences into new configurations that allow better predictions to be made about reality. Those expectations that are 'fit' tend to survive, while those that are 'unfit' tend to be weeded out. This selection process clearly has a counterpart operating at the social level. As will be seen, the role of the judge consists of upholding those rules that will 'maximize' the matching of expectations. Rules in effect draw the demarcation line between 'legitimate' expectations and 'illegitimate' expectations, thus defining the kind of expectations that can be expected to enjoy social protection. On all levels expectations have a tendency towards coherence and coordination. The criterion of fitness is

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confirmation of expectations as indicated by the success of our actions. Expectations more consistent with social reality give a competitive advantage to the individuals holding them. Rules are thus valued for instrumental reasons.

It is Hayek's emphasis on the theme of the interrelation between the system of rules and its systematic outcome at the level of the order of actions that qualifies him as a law and economics theorist (see also Hayek, 1967 pp. 66–81). In a sense the theme of the interplay between institutional structure and economic order was, at least implicitly, already touched upon in Hayek's early economic work. Thus in the so-called 'Austrian' theory of the trade cycle (Hayek, 1931) the boom is a self-reversing process set into motion by monetary expansion brought about by the central bank, which is essentially a governmental bank. If the banks were truly competitive, the business cycle would never get under way.

Spontaneous order and the theory of cultural evolution

The problem of social learning has two aspects which, though they cannot be sharply separated, are nevertheless distinct (see also Hayek, 1960, ch. II, esp. p. 27). First there is the cross-sectional problem of using and communicating the fractional knowledge that is dispersed among the individual contemporaries in a society. This aspect is the subject of Hayek's theory of the spontaneous order of the market which is best known for its emphasis on the capacity of markets to utilize dispersed knowledge. Markets are polycentric orders. They can be seen as continuing, open-ended processes of trial-and-error elimination, processes in which constantly a multiplicity of independent trials, of conjectural problem solutions are tried out and selected through the choices of market participants. Through the interaction of experimental exploration and competitive selection markets can be expected to generate a cumulative growth of problem-solving knowledge. Hayek's notion of competition as a 'discovery procedure' (see Hayek, 1978, pp. 179–90) alludes to this role of the market as an evolutionary learning process.

Hayek's theory of the spontaneous order of the market delivers the insight that, if we want to generate in society any particular order of a certain degree of complexity, we should look for general rules of conduct which, if followed by individuals, would tend to induce that order to form spontaneously. Such a spontaneous or polycentric order rests on a 'division of knowledge' which is analogous with the division of labour in classical economic theory. Because each individual makes use of his or her specific knowledge in deciding how to act, spontaneous orders embody a totality of knowledge that is not known to any single mind. Via the insight that a spontaneous order utilizes much more knowledge than can possibly be made accessible to any central agent or agency, the theory gives us reasons for doubting the ability of governments to

achieve complex feats of social organization by deliberate planning. At the same time the theory amounts to an instrumental justification of a particular type of rules. Spontaneous orders emerge out of the interaction of a multiplicity of elements which, in their responses to their particular environment, are governed by certain general rules. The individuals themselves may be unable to articulate the rules they follow. However, the rules of just conduct on which spontaneous orders rely exhibit certain structural characteristics that make them conceptually distinct from rules of organization. They are negative, purpose-independent, abstract, universal and permanent. The character of these rules will permit the inference only of the general features of the overall pattern. The particular content of the resulting order will always be dependent on the specific circumstances to which the elements respond and consequently will be unpredictable. Furthermore, it should be noted that the specification of the criteria that rules must meet in order to allow for the formation of a spontaneous social order remains, equally, very general. In fact, Hayek's account offers only a very general schema which has to be filled in in detail.

The theory of the market, or the catallaxy, is only one part of Hayek's idea of an evolutionary process of collective learning. The second aspect is concerned with the accumulation and growth of knowledge over time, that is the intertemporal problem of profiting from experiences that previously living generations have had. With regard to the intertemporal dimension of the use-of-knowledge problem, Hayek has advanced a theory of cultural evolution. At the core of this theory is the notion that 'the various institutions and habits, tools and methods of doing things, which ... constitute our inherited civilization' (Hayek, 1960, p. 62) have passed 'the slow test of time' (Hayek, 1967, p. 111) and can, therefore, be expected to embody the experience of generations. They are, as Hayek argues, the 'product of long experimentation in the past' (Hayek, 1978, p. 136) and 'embody the experience of many more trials and errors than any individual mind could acquire' (Hayek, 1967, p. 88). What is distinctive in Hayek's theory is his account of social institutions and rules of conduct as 'bearers of knowledge' (Kukathas, 1989, p. 220).

The rules and institutions that define the frameworks within which social interactions take place embody knowledge of which we are otherwise unaware because they are themselves the outcome of a process of competitive selection. The abstract frameworks which contribute to the formation of spontaneous orders – basically the rules of the law of property, tort and contract (see Hayek, 1976, p. 109) – are thus themselves conceptualized as more or less unintended products of an evolutionary process. Thus Hayek sees common law both as a codification of previously unarticulated rules of conduct and as providing a framework within which spontaneous orders can form.

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As Vanberg points out (Vanberg, 1994, *passim*), Hayek's theory of cultural evolution becomes disputable where it seems to argue that because of our 'incurable ignorance' we ought necessarily to rely largely on unquestioned traditional rules instead of attempting to choose rationally or to construct the system of rules that we want to follow.

The question of how the different kinds of rules differ in their nature – rules of conduct versus organizational rules – must be distinguished from the question of how they originate – whether they 'spontaneously evolve' or are 'deliberately designed'. In a particular sociohistorical situation there may exist a de facto correlation between the two aspects, but this need not be so. The two dimensions are conceptually distinct. This fact was acknowledged by Hayek (see Hayek, 1973, pp. 45–6).

The evolution of common law and the role of the judge

As has already been pointed out, a central theme in Hayek's system of thought refers to the interplay between the order of rules and the order of actions. Hayek distinguishes between the legal framework, upon which the relative certainty of expectations is founded, and the system of market exchanges within that framework, in which there is no certainty of expectations. Because of the stability of the legal framework, agents can rely on expectations regarding the typical form or pattern of economic interactions. In contract law, for example, there are criteria for a valid contract regardless of the price or nature of the goods exchanged. But within this overall pattern equilibrium at the level of legal institutions, there is a disequilibrium or continual change in the economic variables. Agents will continually change their plans in accordance with new facts about both the external world and other agents. In fact, the stable legal framework, in facilitating such changes, ensures maximum market coordination. In other words, maximum coordination – the highest possible degree of coordination – does not necessarily mean a state of full or exact coordination. The very process of coordinating must involve a certain amount of (adaptive) discoordination.

Moreover, the stability of the legal framework is not absolute. As will be seen, the rules themselves evolve. Hayek's account of the role of the common law judge is very illuminating in this respect. In Hayek's theory of the common law and the role of the judge, the emphasis is on the coordination of individual activities through a process of systematic mutual adjustment of expectations (Hayek, 1973, p. 86). The function of the judge is to ensure a maximal coincidence of (legitimate) expectations, that is, to create a situation in which the chance to form correct expectations is as great as possible. But the chance of as many expectations as possible being fulfilled will be best enhanced if some expectations are allowed to be systematically disappointed.

Thus the judges, by upholding those rules which make it more likely that expectations will match and not conflict, are consciously trying to give greater internal coherence to the law. However, they do not need to know anything about the nature of the resulting overall order which they serve, beyond the fact that the rules are meant to assist the individuals in successfully forming expectations in a wide range of circumstances. They are unintentionally playing a part in the formation of a spontaneous order: a system of rules of conduct conducive to the efficient operation of the order of actions which rests on it. The body of the common law constitutes a spontaneous order, which evolves as an unintended consequence of the following of meta-rules. One of the most fundamental meta-rules is that, when deciding a difficult case, the judge's task is to try to make the law as a whole a little more coherent: he is required to think only about the internal logic of the law. But this is probably less true with respect to the law in Europe, which is more constrained by laws and articles than with respect to the common law in the United States and Great Britain, where the common law is formed by cases.

The judge assists in the process of selection of rules. In fact, three distinct evolutionary mechanisms are involved in Hayek's account of the *modus operandi* of the judiciary. If there were no variation, evolution could not get started as a result of selection. At first sight, however, there seems to be little room for a *variation or mutation mechanism* in Hayek's account of the judge's task. The judge will merely assist in 'the process of articulation of pre-existing rules' (Hayek, 1973, p. 78). The judge 'is committed to upholding the principles on which the existing order is based' (*ibid.*, p. 120). He discovers the rules 'presumed to have guided expectations in many similar situations in the past' (*ibid.*, p. 86). The judge 'is not a creator of a new order but a servant endeavouring to maintain and improve the functioning of an existing order' (*ibid.*, p. 119). 'The task of the judge will be to tell the parties in the dispute what ought to have guided their expectations, ... because this was the established custom which they ought to have known' (*ibid.*, p. 87). Thus the emphasis is laid on the fact that judges adjudicate particular cases by means of custom and precedent. This is what is meant by *stare decisis*, which can be said to account for the *transmission or replication mechanism* in the evolution of the law.

How then does variation arise? 'Experience will often prove that in new situations rules which have come to be accepted lead to conflicting expectations' (*ibid.*, p. 115). And further: 'Since new situations in which the established rules are not adequate will constantly arise, the task of preventing conflict and enhancing the compatibility of actions (...) is of necessity a never-ending one, requiring (...) the formulation of new rules necessary for the preservation of the order of actions' (*ibid.*, p. 119). Thus variation is generated.

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But 'This will in some measure always be an experimental process, since the judge (...) will never be able to foresee all the consequences of the rule he lays down, and will often fail in his endeavour to reduce the sources of conflicts of expectations' (ibid., p. 102). And 'The judge may err' (ibid., p. 119).

By what mechanism are errors, that is, unfit rules, eliminated? It is 'only by their effects on that order of actions, effects which will be discovered only by trial and error, that the adequacy or inadequacy of the rules can be judged' (ibid., p. 102). 'Like most other intellectual tasks, that of the judge is (...) one of testing hypotheses at which he has arrived by processes only in part conscious. (...) he must stand by his decision only if he can rationally defend it against all objections that can be raised against it' (ibid., p. 120). 'As in all other fields advance is here achieved by our moving within an existing system of thought and endeavouring by a process of piecemeal tinkering, or "immanent criticism", to make the whole more consistent both internally as well as with the facts to which the rules are applied' (ibid., p. 118). Thus a learning process of trial-and-error elimination accounts for *the selection mechanism*.

Law and legislation

Hayek clearly recognized that 'the spontaneous process of growth may lead into an impasse from which it cannot extricate itself by its own forces' (Hayek, 1973, p. 88). It is therefore acknowledged that grown law requires correction by legislation. It seems that legislation may be required both to generate novelty – that is, legislation works as a mutation mechanism – and to eliminate errors in past developments – that is, it also works as a selection mechanism.

The insight that spontaneous growth will not necessarily operate to generate efficient results is corroborated by the game-theoretic analysis of invisible hand processes. The institutions that develop may be sub-optimal in nature and they need not be efficient to persist. For example, in impure coordination games, the players may get stuck in a self-enforcing Nash equilibrium that is not Pareto-efficient and thus sub-optimal self-sustaining conventions may evolve.

The rule of law

Hayek undertakes to show that the operation of the market leads not only to the creation of an order, but also to a great increase in the return which men receive from their efforts. 'The game of catallaxy' is a wealth-creating game, that is, one that leads to an increase in the stream of goods and in the prospects of all participants to satisfy their needs (Hayek, 1976, p. 115). However, the tendency of the market to promote welfare is subject to some qualifications. Hayek accepts that the state should provide a safety net of

which is different from the governmental assembly entrusted with the task of government. The coercive powers of the latter assembly would be limited by the rules of justice laid down by the first. Thus a true separation of powers would be achieved. The basic clause of such a constitution would have to state that in normal times men could be restrained from doing what they wished, or coerced to do particular things, only in accordance with the recognized rules of just conduct designed to define and protect the individual domain of each. Practical difficulties are worked out through a special constitutional court.

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